

Research Economy Watch

17 July 2025

Inflation to test the top of RBNZ target band

- **Monthly prices support higher near-term inflation view**
- **We maintain our 0.8% q/q, 2.9% y/y CPI forecast for Q2**
- **And 3.0% y/y pick for Q3**
- **Food, electricity prices rising sharply**
- **Rent inflation easing**

Today's June Selected Price Indexes support our view that Q2 CPI inflation will print above the RBNZ's MPS forecasts and sets up a further nudge higher in Q3.

The balance of the volatile monthly prices came in a touch stronger than our assumptions for the month although not enough to alter our pick for next Monday's Q2 CPI.

Our Q2 CPI forecast remains at +0.8% q/q and 2.9% y/y. This is stronger than the RBNZ's May MPS forecast of 0.5% q/q and 2.6% y/y.

Of course, the Q2 CPI inflation outcome also depends on the remaining 53%+ of the index not covered by the Selected Monthly Indexes.

It is also important to note that today's June prices set a marginally higher than expected base heading into Q3. Like Q2, it is not enough to change our forecast for that quarter, but it maintains a sense of upward near-term pressure. We already forecast annual inflation to lift to 3.0% in Q3 (and stay there in Q4).

The RBNZ openly acknowledged near term inflation upside in its July MPR noting that 'inflation is expected to increase further in the June and September quarters toward the top of the MPC's inflation target band.' And the Bank still confirmed an easing bias.

So higher near-term inflation remains a risk to monitor but need not necessarily derail further reduction in the OCR if the RBNZ continues to look through the near-term pressure and focus on a subdued medium-term outlook.

However, if higher near-term inflation were to stick around for too long it raises the risk of having more influence on inflation expectations. That would be something that the RBNZ would be concerned about.

The RBNZ had noted the near-term increase in inflation is due to a pick-up in food prices and elevated administered price increases.

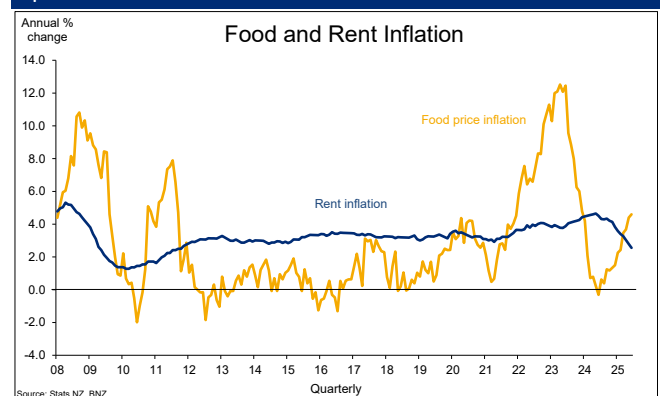
There were signs of this in today's figures. Food prices rose 1.2% m/m in June, taking their annual inflation up to 4.6%.

This was a bit higher than we had pencilled in. We expect annual food price inflation to remain elevated in 2025 given previous increases in commodity prices and their usual lag to retail pricing. Global food price inflation is starting to ease and would take some heat out of retail price rises into next year if historical patterns hold.

While that would help on the inflation front in due course, it is also important to recognise the hit to household disposable income that comes with elevated prices. It is another reason to not expect a rapid recovery in real household spending.

Food prices accounted for the majority of the upside surprise to our monthly assumptions, with the remainder coming from highly volatile components like airfares and accommodation prices. The latter's 1.4% m/m decline not as much as we had pencilled in. There is a good chance that movements in these volatile components unwind over subsequent months.

Ups and downs



Some other prices were a touch weaker than we had factored in. Electricity prices rose 1.6% m/m, another firm increase but not quite as much as in recent months or as much as we had factored in. Still, electricity prices are up a hefty 10.4% y/y – another material draw on household disposable incomes.

Rent inflation continues to ease. The 0.1% m/m was a tick lower than our assumption for the month but strongly supports our view that annual rent inflation is tracking firmly downward. Annual rent inflation has already slowed

to 2.6% (its lowest since 2011) and we think it has further to go.

Softening rent inflation is an important component of the further easing we anticipate in non-tradeables inflation over coming quarters. That is in stark contrast to a sharp lift expected in tradeable inflation, reflecting higher food prices among other factors.

Other minor downside surprises in today's data came from alcoholic beverages and cigarettes, while fuel prices were not far from our priors.

doug_steel@bnz.co.nz

Contact Details

BNZ Research

Stephen Toplis Head of Research	Doug Steel Senior Economist	Matt Brunt Economist	Jason Wong Senior Markets Strategist	Stuart Ritson Senior Interest Rate Strategist
Mike Jones BNZ Chief Economist				

Main Offices

Wellington Level 2, BNZ Place 1 Whitmore St Private Bag 39806 Wellington Mail Centre Lower Hutt 5045 New Zealand Toll Free: 0800 283 269	Auckland 80 Queen Street Private Bag 92208 Auckland 1142 New Zealand Toll Free: 0800 283 269	Christchurch 111 Cashel Street Christchurch 8011 New Zealand Toll Free: 0800 854 854
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